
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2005

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 1-13395

SONIC AUTOMOTIVE, INC.

(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of
incorporation or organization)

6415 Idlewild Road, Suite 109, Charlotte, North Carolina
(Address of principal executive offices)

56-2010790
(I.R.S. Employer
Identification No.)

28212
(Zip Code)

(704) 566-2400
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of April 29, 2005, there were 29,655,990 shares of Class A Common Stock and 12,029,375 shares of Class B Common Stock outstanding.

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PART I - FINANCIAL INFORMATION

Item 1: Condensed Consolidated Financial Statements.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Dollars and shares in thousands except per share amounts)
(Unaudited)

	Three-Month Periods Ended March 31,	
	2004	2005
Revenues:		
New vehicles	\$ 995,123	\$1,079,383
Used vehicles	285,657	305,860
Wholesale vehicles	111,096	126,282
Total vehicles	1,391,876	1,511,525
Parts, service and collision repair	242,895	267,415
Finance, insurance and other	43,330	46,536
Total revenues	1,678,101	1,825,476
Cost of sales	1,413,037	1,538,135
Gross profit	265,064	287,341
Selling, general and administrative expenses	210,529	232,125
Depreciation and amortization	3,572	4,082
Operating income	50,963	51,134
Other income / (expense):		
Interest expense, floor plan	(5,865)	(9,028)
Interest expense, other, net	(9,702)	(11,130)
Other income, net	28	17
Total other expense	(15,539)	(20,141)
Income from continuing operations before income taxes	35,424	30,993
Provision for income taxes	13,171	11,622
Income from continuing operations	22,253	19,371
Discontinued operations:		
Loss from operations and the sale of discontinued franchises	(248)	(3,615)
Income tax benefit	180	1,356
Loss from discontinued operations	(68)	(2,259)
Net income	\$ 22,185	\$ 17,112
Basic earnings (loss) per share:		
Earnings per share from continuing operations	\$ 0.54	\$ 0.46
Loss per share from discontinued operations	—	(0.05)
Earnings per share	\$ 0.54	\$ 0.41
Weighted average common shares outstanding	41,193	41,748
Diluted earnings (loss) per share:		
Earnings per share from continuing operations	\$ 0.51	\$ 0.45
Loss per share from discontinued operations	—	(0.05)
Earnings per share	\$ 0.51	\$ 0.40
Weighted average common shares outstanding	45,375	45,460
Dividends declared per common share	\$ 0.10	\$ 0.12

See notes to unaudited condensed consolidated financial statements.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Dollars in thousands)

	<u>December 31,</u> <u>2004</u>	<u>March 31,</u> <u>2005</u> <u>(Unaudited)</u>
ASSETS		
Current Assets:		
Cash	\$ 9,991	\$ 5,974
Receivables, net	357,403	330,764
Inventories	1,024,342	1,061,865
Assets held for sale	98,530	96,400
Other current assets	101,277	112,104
Total current assets	<u>1,591,543</u>	<u>1,607,107</u>
Property and equipment, net	134,490	139,344
Goodwill, net	1,056,924	1,065,003
Other intangible assets, net	84,777	87,206
Other assets	33,877	35,981
Total assets	<u>\$ 2,901,611</u>	<u>\$ 2,934,641</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Notes payable - floor plan	\$ 984,549	\$ 985,019
Trade accounts payable	88,616	87,466
Accrued interest	15,421	12,067
Other accrued liabilities	175,510	157,383
Liabilities held for sale	66,309	65,877
Current maturities of long-term debt	2,970	3,016
Total current liabilities	<u>1,333,375</u>	<u>1,310,828</u>
Long-term debt	668,826	707,556
Other long-term liabilities	28,888	31,299
Deferred income taxes	100,835	101,256
Stockholders' Equity:		
Class A Common Stock; \$.01 par value; 100,000,000 shares authorized; 39,979,567 shares issued and 29,631,703 shares outstanding at December 31, 2004; 40,113,547 shares issued and 29,698,183 shares outstanding at March 31, 2005	397	398
Class B Common Stock; \$.01 par value; 30,000,000 shares authorized; 12,029,375 shares issued and outstanding at December 31, 2004 and March 31, 2005	121	121
Paid-in capital	441,503	443,970
Retained earnings	470,663	482,736
Accumulated other comprehensive loss	(1,228)	(569)
Deferred compensation related to restricted stock	(3,408)	(3,089)
Treasury Stock, at cost (10,347,864 Class A shares held at December 31, 2004 and 10,415,364 Class A shares held at March 31, 2005)	(138,361)	(139,865)
Total stockholders' equity	<u>769,687</u>	<u>783,702</u>
Total liabilities and stockholders' equity	<u>\$ 2,901,611</u>	<u>\$ 2,934,641</u>

See notes to unaudited condensed consolidated financial statements.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(Dollars and shares in thousands)
(Unaudited)

	Class A Common Stock		Class B Common Stock		Deferred Compensation Related to Restricted Stock	Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Shares	Amount	Shares	Amount						
Balance at December 31, 2004	39,980	\$ 397	12,029	\$ 121	\$ (3,408)	\$ 441,503	\$ 470,663	\$ (138,361)	\$ (1,228)	\$ 769,687
Comprehensive Income:										
Net income							17,112			17,112
Change in fair value of interest rate swap, net of tax expense of \$421									659	659
Total comprehensive income, net of tax										17,771
Shares issued under stock compensation plans	134	1				2,313				2,314
Restricted stock amortization					319					319
Income tax benefit associated with stock compensation plans						154				154
Dividends declared							(5,039)			(5,039)
Purchases of treasury stock								(1,504)		(1,504)
Balance at March 31, 2005	40,114	\$ 398	12,029	\$ 121	\$ (3,089)	\$ 443,970	\$ 482,736	\$ (139,865)	\$ (569)	\$ 783,702

See notes to unaudited condensed consolidated financial statements.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)
(Unaudited)

	Three Months Ended March 31,	
	2004	2005
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 22,185	\$ 17,112
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization of property and equipment	3,659	4,144
Other amortization	73	70
Debt issue cost amortization	87	100
Debt discount / (premium) amortization, net	182	(28)
Restricted stock amortization	—	319
Equity interest in gains of investee	(164)	(200)
(Gain) / Loss on disposal of assets, including franchises	(708)	672
Income tax benefit associated with stock compensation plans	678	154
Changes in assets and liabilities that relate to operations:		
Receivables	(4,452)	26,638
Inventories	(54,006)	(32,408)
Other assets	(12,196)	(5,596)
Notes payable - floor plan	30,781	(4,345)
Trade accounts payable and other liabilities	11,647	(22,147)
Total adjustments	(24,419)	(32,627)
Net cash used in operating activities	(2,234)	(15,515)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of businesses, net of cash acquired	(58,569)	(11,841)
Purchases of property and equipment	(21,338)	(21,737)
Proceeds from sales of property and equipment	15,066	6,074
Proceeds from sales of franchises	30,462	1,735
Net cash used in investing activities	(34,379)	(25,769)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net borrowings on revolving credit facilities	588	42,024
Payments on long-term debt	(398)	(564)
Purchases of treasury stock	(4,471)	(1,504)
Issuance of shares under stock compensation plans	2,407	2,314
Dividends paid	(4,120)	(5,003)
Net cash (used in)/provided by financing activities	(5,994)	37,267
NET DECREASE IN CASH	(42,607)	(4,017)
CASH, BEGINNING OF PERIOD	82,082	9,991
CASH, END OF PERIOD	\$ 39,475	\$ 5,974
SUPPLEMENTAL SCHEDULE OF NON-CASH FINANCING ACTIVITIES:		
Change in fair value of cash flow hedging instruments (net of tax benefit of \$51 for the three months ended March 31, 2004 and net of tax expense of \$421 for the three months ended March 31, 2005)	\$ (80)	\$ 659
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid for interest, net of amount capitalized	\$ 20,076	\$ 24,982
Cash paid for income taxes	\$ 299	\$ 11,558

See notes to unaudited condensed consolidated financial statements.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation - The accompanying unaudited financial information for the three months ended March 31, 2005 has been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. All significant intercompany accounts and transactions have been eliminated. These unaudited condensed consolidated financial statements reflect, in the opinion of management, all material adjustments (which include only normal recurring adjustments) necessary to fairly state the financial position and the results of operations for the periods presented. The results for interim periods are not necessarily indicative of the results to be expected for the entire fiscal year. These interim financial statements should be read in conjunction with the audited consolidated financial statements of Sonic for the year ended December 31, 2004, which were included in Sonic's Annual Report on Form 10-K.

Stock-Based Compensation - Sonic accounts for stock-based compensation plans under the recognition and measurement provisions of APB Opinion No. 25, "Accounting for Stock Issued to Employees", and related interpretations. In accordance with those provisions, because the exercise price of all options granted under those plans equaled the market value of the underlying stock at the grant date, no stock-based employee compensation cost is recorded in the accompanying unaudited condensed consolidated financial statements. Using the Black-Scholes option pricing model for all options granted, the following table illustrates the effect on net income and earnings per share if Sonic had applied the fair value recognition provisions of SFAS No. 123, "Accounting for Stock-Based Compensation", to stock-based employee compensation:

	(Dollars in thousands except per share amounts)	
	Three Months Ended March 31,	
	2004	2005
Net income as reported	\$ 22,185	\$ 17,112
Fair value compensation cost, net of tax benefits of \$1,148 and \$884, for the three months ended March 31, 2004 and 2005, respectively	(1,960)	(1,473)
Pro forma net income	\$ 20,225	\$ 15,639
Basic earnings (loss) per share:		
Earnings as reported	\$ 0.54	\$ 0.41
Fair value compensation cost, net of tax benefit	(0.05)	(0.04)
Pro forma earnings per share	\$ 0.49	\$ 0.37
Diluted earnings (loss) per share:		
Earnings as reported	\$ 0.51	\$ 0.40
Fair value compensation cost, net of tax benefit	(0.04)	(0.03)
Pro forma earnings per share	\$ 0.47	\$ 0.37

Reclassifications - Loss from operations and the sale of discontinued franchises for the three month period ended March 31, 2004 reflects reclassifications from the prior year presentation to include additional franchises sold and terminated or identified for sale subsequent to March 31, 2004 which had not been previously included in discontinued operations and exclude franchises which had been identified for sale as of March 31, 2004 but which Sonic has decided to retain and operate as of March 31, 2005. In addition, in order to maintain consistency and comparability between periods, certain other amounts in Sonic's accompanying unaudited condensed consolidated financial statements have been reclassified from previously reported balances to conform to the current period classification. These reclassifications primarily relate to the presentation of assets and liabilities for franchises classified as held for sale and real estate and construction costs expected to be sold in one year in sale-leaseback transactions in the accompanying unaudited condensed consolidated balance sheets.

Recent Accounting Pronouncements - In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment" which replaces SFAS No. 123 and supercedes APB 25. SFAS No. 123R requires a public entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost will be recognized over the period during which an employee is required to provide service in exchange for the award (usually the vesting period). Tax benefits associated with share-based payments will be recognized as an addition to paid-in capital. Cash retained as a result of these tax benefits will be presented in the statement of cash flows as financing cash inflows. Sonic is currently evaluating the provisions of SFAS No. 123R, which will be effective for the first quarter of 2006, and has not determined the impact on Sonic's consolidated operating results, financial position and cash flows.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

2. BUSINESS ACQUISITIONS AND DISPOSITIONS

Acquisitions:

The aggregate purchase price for franchises acquired during the first quarter of 2005 totaled approximately \$11.8 million in cash, net of cash acquired, and was funded by cash from operations and borrowings under the revolving credit facility. The unaudited condensed consolidated balance sheet as of March 31, 2005 includes preliminary allocations of the purchase price of the acquisition to the assets and liabilities acquired based on their estimated fair market values at the date of acquisition and are subject to final adjustment. As a result of these allocations, Sonic has recorded the following:

- \$1.8 million of net assets relating to dealership operations;
- \$2.3 million of intangible assets representing rights acquired under franchise agreements; and
- \$7.7 million of goodwill, all of which is expected to be tax deductible.

Dispositions:

During the first quarter of 2005, Sonic sold two franchises. These disposals generated cash of \$1.7 million and resulted in a net loss of \$0.9 million, which is included in discontinued operations in the accompanying unaudited condensed consolidated statement of income for the quarter ended March 31, 2005.

In conjunction with franchise dispositions, Sonic generally agrees to indemnify the buyers from certain liabilities and costs arising from operations or events that occurred prior to sale but which may or may not be known at the time of sale, including environmental liabilities and liabilities associated from the breach of representations or warranties made under the agreements. The additional exposure associated with dispositions in the three month period ended March 31, 2005 related to subleases was \$0.9 million. However, Sonic's maximum exposure associated with general indemnifications increased by \$6.3 million as a result of these dispositions. These indemnifications expire within a period of one to three years following the date of the sale. The estimated fair value of these indemnifications was not material.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In addition to the dispositions described above, as of March 31, 2005, Sonic has identified 22 additional franchises that were held for sale. These franchises are generally franchises with unprofitable operations that Sonic expects to dispose of during 2005. The operating results of these franchises are included in discontinued operations in the accompanying unaudited condensed consolidated statements of income. Assets to be disposed of in connection with franchises not yet sold, which have been classified in assets held for sale in the accompanying unaudited condensed consolidated balance sheets, consist of the following:

	(Dollars in thousands)	
	December 31, 2004	March 31, 2005
Inventories	\$ 70,715	\$ 70,703
Property and equipment:		
Building and improvements	8,516	7,861
Office equipment and fixtures	3,200	2,954
Parts and service equipment	3,685	3,548
Company vehicles	406	435
Construction in progress	446	435
	<u>16,253</u>	<u>15,233</u>
Total property and equipment, cost	16,253	15,233
Less accumulated depreciation	(2,197)	(2,016)
	<u>14,056</u>	<u>13,217</u>
Total property and equipment, net	14,056	13,217
Goodwill	8,259	6,980
Franchise assets	5,500	5,500
	<u>98,530</u>	<u>96,400</u>
Assets held for sale	\$ 98,530	\$ 96,400

Liabilities to be disposed in connection with these dispositions are comprised entirely of notes payable – floor plan and are classified as liabilities held for sale on the accompanying unaudited condensed consolidated balance sheets. Revenues associated with franchises classified as discontinued operations were \$110.4 million for the three month period ended March 31, 2005 and \$150.5 million for the three month period ended March 31, 2004. The pre-tax losses (before gains or losses on the sale of disposed franchises) associated with franchises classified as discontinued operations were \$3.6 million for the three month period ended March 31, 2005 and \$0.2 million for the three month period ended March 31, 2004.

3. INVENTORIES

Inventories consist of the following:

	(Dollars in thousands)	
	December 31, 2004	March 31, 2005
New vehicles	\$ 848,197	\$ 860,438
Used vehicles	130,354	150,390
Parts and accessories	53,932	56,171
Other	62,574	65,569
	<u>1,095,057</u>	<u>1,132,568</u>
Less assets held for sale	(70,715)	(70,703)
Inventories	<u>\$ 1,024,342</u>	<u>\$ 1,061,865</u>

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

4. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	(Dollars in thousands)	
	December 31, 2004	March 31, 2005
Land	\$ 6,104	\$ 3,874
Building and improvements	81,720	82,353
Office equipment and fixtures	43,188	44,379
Parts and service equipment	30,793	32,207
Company vehicles	8,715	9,257
Construction in progress	6,340	13,264
Total, at cost	176,860	185,334
Less accumulated depreciation	(42,370)	(45,990)
Property and equipment, net	\$ 134,490	\$139,344

In addition to the amounts shown above, Sonic incurred approximately \$77.4 million in real estate and construction costs as of December 31, 2004 and \$84.5 million as of March 31, 2005 on dealership facilities that are or were expected to be completed and sold within one year in sale-leaseback transactions. Accordingly, these costs are included in other current assets on the accompanying unaudited condensed consolidated balance sheets. Under the terms of the sale-leaseback transactions, Sonic sells the dealership facilities to unaffiliated third parties and enters into long-term operating leases on the dealership facilities. During the first three months of 2005, Sonic sold dealership facilities with a carrying value of \$1.9 million in sale-leaseback transactions. Gains and losses from these sale-leaseback transactions were not material.

5. GOODWILL AND INTANGIBLE ASSETS

The changes in the carrying amount of franchise agreements and goodwill for the three months ended March 31, 2005 were as follows:

	(Dollars in thousands)	
	Franchise Agreements	Goodwill
Balance before assets held for sale classification, December 31, 2004	\$ 86,000	\$1,065,184
Amount classified as assets held for sale	(5,500)	(8,260)
Balance, December 31, 2004	80,500	1,056,924
Additions through current year acquisitions	2,300	7,723
Prior year acquisition allocations	200	40
Reductions from sales of franchises	—	(963)
Sub-total, March 31, 2005	83,000	1,063,724
Decrease in amount classified as assets held for sale	—	1,279
Balance, March 31, 2005	\$ 83,000	\$1,065,003

Franchise agreements and definite life intangible assets (\$4.2 million and \$4.3 million at March 31, 2005 and December 31, 2004, respectively) are classified as Other intangible assets, net on the accompanying unaudited condensed consolidated balance sheets.

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SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

6. LONG-TERM DEBT

Long-term debt consists of the following:

	(Dollars in thousands)	
	December 31, 2004	March 31, 2005
\$550 million revolving credit facility bearing interest at 2.55 percentage points above LIBOR and maturing October 31, 2006, collateralized by all of Sonic's assets	\$ 238,633	\$280,657
Senior Subordinated Notes bearing interest at 8.625%, maturing August 15, 2013, net of net discount of \$3,065 and \$3,004, respectively	271,935	271,996
Convertible Senior Subordinated Notes bearing interest at 5.25%, maturing May 7, 2009, net of discount of \$2,606 and \$2,473, respectively	127,494	127,627
Notes payable to a finance company bearing interest from 10.52% to 9.52% (with a weighted average of 10.19%), with combined monthly principal and interest payments of \$325, maturing November 1, 2015 through September 1, 2016, and collateralized by letters of credit with a commercial bank, including premiums of \$6,583 and \$6,360, respectively (1)	32,369	31,726
Fair value of variable interest rate swaps	(145)	(2,937)
Other notes payable (primarily equipment notes)	1,510	1,503
	<u>\$ 671,796</u>	<u>\$710,572</u>
Less: current maturities	(2,970)	(3,016)
Long-term debt	<u>\$ 668,826</u>	<u>\$707,556</u>

(1) Notes payable were assumed in connection with acquisitions during 2004 and were recorded at fair value using an interest rate of 5.35%.

The indenture governing Sonic's 8.625% senior subordinated notes limits Sonic's ability to pay quarterly cash dividends in excess of \$0.10 per share. Sonic may only pay quarterly cash dividends in excess of this amount if Sonic complies with Section 1009 of the indenture governing these notes, which was filed as Exhibit 4.4 to the Registration Statement on Form S-4 (Reg. No. 333-109426). The indenture governing Sonic's convertible senior subordinated notes (the "Convertibles") does not limit Sonic's ability to pay dividends. Sonic's credit agreement permits cash dividends so long as no event of default or unmatured default (as defined in the credit agreement for the Convertibles) has occurred and is continuing and provided that, after giving effect to the payment of a dividend, Sonic remains in compliance with the other terms and conditions of the credit agreement.

Neither of the conversion features on the Convertibles were satisfied during the three months ended March 31, 2005. Sonic was in compliance with all financial covenants under the above long-term debt and credit facilities as of March 31, 2005.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

7. PER SHARE DATA

The calculation of diluted net income per share considers the potential dilutive effect of Sonic's contingently convertible debt and stock options under Sonic's stock compensation plans. The following table illustrates the dilutive effect of such items:

	(Shares in thousands) Three Months Ended March 31,	
	2004	2005
Basic weighted average number of common shares outstanding	41,193	41,748
Effect of dilutive securities:		
Contingently convertible debt	2,776	2,776
Stock compensation plans	1,406	936
Weighted average number of common shares outstanding, including effect of dilutive securities	45,375	45,460

In addition to the stock options included in the table above, options to purchase 1.7 million shares and 1.9 million shares of Class A common stock were outstanding during the three month periods ended March 31, 2004 and 2005, respectively, but were not included in the computation of diluted net income per share because the options were antidilutive. The total amount of stock options outstanding at March 31, 2004 and 2005 were 7.0 million and 6.3 million, respectively.

8. CONTINGENCIES**Legal Proceedings:**

Sonic is involved, and will continue to be involved, in numerous legal proceedings arising in the ordinary course of business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities.

Several of Sonic's Texas dealership subsidiaries have been named in three class action lawsuits brought against the Texas Automobile Dealers Association ("TADA") and new vehicle dealerships in Texas that are members of the TADA. Approximately 630 Texas dealerships are named as defendants in two of the actions, and approximately 700 Texas dealerships are named as defendants in the other action. The three actions allege that since January 1994, Texas automobile dealerships have deceived customers with respect to a vehicle inventory tax and violated federal antitrust and other laws. In two of the actions, the Texas state court certified two classes of consumers on whose behalf the actions would proceed. The Texas Court of Appeals has affirmed the trial court's order of class certification in the state actions, and the Texas Supreme Court issued an order for the second time in September 2004 stating that it would not hear the merits of the defendant's appeal on class certification. The federal trial court conditionally certified a class of consumers in the federal antitrust case, but on appeal by the defendant dealerships, the U.S. Court of Appeals for the Fifth Circuit reversed the certification of the plaintiff class in October 2004 and remanded the case back to the federal trial court for further proceedings not inconsistent with the Fifth Circuit's ruling. The plaintiffs in the federal lawsuit are seeking to have the U.S. Supreme Court hear an appeal of the Fifth Circuit's ruling that reversed the federal trial court's class certification order.

If the TADA matters are not settled, Sonic and its dealership subsidiaries intend to vigorously defend themselves and assert available defenses. In addition, Sonic may have rights of indemnification with respect to certain aspects of the TADA matters. However, an adverse resolution of the TADA matters may result in the payment of significant costs and damages, which could have a material adverse effect on Sonic's future results of operations and cash flows.

In addition to the TADA matters described above, Sonic is involved in numerous other legal proceedings arising out of the conduct of Sonic's business. Sonic's management does not believe that the ultimate resolution of these legal proceedings will have a material adverse effect on the Company's business, financial condition, results of operations, cash flows or prospects. However, the results of these legal proceedings cannot be predicted with certainty, and an unfavorable resolution of one or more of these legal proceedings could have a material adverse effect on Sonic's business, financial condition, results of operations cash flows and prospects. Included in other accrued liabilities at December 31, 2004 and March 31, 2005 are \$2.9 million and \$2.5 million, respectively, in reserves that Sonic has provided for these matters.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Guarantees:

In accordance with the terms of Sonic's operating lease agreements, Sonic's dealership subsidiaries, acting as lessees, generally agree to indemnify the lessor from certain exposure arising as a result of the use of the leased premises, including environmental exposure and repairs to leased property upon termination of the lease. In addition, Sonic has generally agreed to indemnify the lessor in the event of a breach of the lease by the lessee.

In connection with franchise dispositions, certain of Sonic's dealership subsidiaries have assigned or sublet to the buyer their interests in real property leases associated with such dealerships. In general, the subsidiaries retain responsibility for the performance of certain obligations under such leases, including rent payments and repairs to leased property upon termination of the lease, to the extent that the assignee or sublessee does not perform. The total estimated rent payments remaining under such leases as of March 31, 2005 was approximately \$54.9 million. However, in accordance with the terms of the assignment and sublease agreements, the assignees and sublessees have generally agreed to indemnify Sonic and its subsidiaries in the event of non-performance. Additionally, in connection with certain dispositions, Sonic has obtained indemnifications from the parent company or owners of these assignees and sublessees in the event of non-performance.

In accordance with the terms of agreements entered into for the sale of our franchises, Sonic generally agrees to indemnify the buyer from certain exposure and costs arising subsequent to the date of sale, including environmental exposure and exposure resulting from the breach of representations or warranties made in accordance with the agreement. While Sonic's exposure with respect to environmental remediation and repairs is difficult to quantify, Sonic estimates that the maximum exposure associated with these general indemnifications was approximately \$21.4 million at March 31, 2005. These indemnifications generally expire within a period of one to three years following the date of sale. The estimated fair value of these indemnifications was not material.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES
MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Item 2: Management’s Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of the results of operations and financial condition should be read in conjunction with the Sonic Automotive, Inc. and Subsidiaries Unaudited Condensed Consolidated Financial Statements and the related notes thereto appearing elsewhere in this report, as well as the audited financial statements and related notes and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” appearing in our Annual Report for the year ended December 31, 2004 on Form 10-K.

Overview

We are one of the largest automotive retailers in the United States. As of April 29, 2005, we owned dealership subsidiaries that operated 187 dealership franchises, representing 38 different brands of cars and light trucks at 156 locations, and 39 collision repair centers in 15 states. Our dealerships provide comprehensive services including sales of both new and used cars and light trucks, sales of replacement parts, performance of vehicle maintenance, warranty, paint and collision repair services, and arrangement of extended service contracts, financing and insurance, vehicle protection products and other aftermarket products (collectively, “F&I”) for our automotive customers. Our brand diversity allows us to offer a broad range of products at a wide range of prices from lower priced, or economy vehicles, to luxury vehicles. We believe that this diversity reduces the risk of changes in customer preferences, product supply shortages and aging products. In addition, although vehicle sales are cyclical and are affected by many factors, including general economic conditions, consumer confidence, levels of discretionary personal income, interest rates and available credit, our parts, service and collision repair services are not closely tied to vehicle sales and are not dependent upon near-term vehicle sales volume. As a result, we believe the diversity of these products and services reduces the risk of periodic economic downturns.

The following is a detail of our new vehicle revenues by brand for the three month periods ended March 31, 2004 and 2005:

Brand (1)	Percentage of New Vehicle Revenues Three Months Ended March 31,	
	2004	2005
Honda	13.2%	13.6%
BMW	10.4%	13.0%
Toyota	12.2%	11.6%
Cadillac	13.1%	10.5%
Ford	10.9%	10.4%
General Motors (2)	11.3%	9.9%
Lexus	6.2%	6.2%
Mercedes	3.4%	3.7%
Volvo	3.7%	3.6%
Nissan	2.9%	2.6%
Chrysler (3)	2.7%	2.4%
Hyundai	1.5%	1.6%
Volkswagen	1.6%	1.5%
Audi	1.0%	1.4%
Other Luxury (4)	4.0%	5.6%
Other (5)	1.9%	2.4%
Total	100.0%	100.0%

- (1) In accordance with the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets”, income statement data reflects reclassifications from the prior years presentation to (1) exclude additional franchises sold and terminated or identified for sale subsequent to March 31, 2004 which had not been previously included in discontinued operations and (2) include franchises which had been identified for sale as of March 31, 2004, but which we have now decided to retain and operate.
- (2) Includes Buick, Chevrolet, GMC, Oldsmobile, Pontiac and Saturn
- (3) Includes Chrysler, Dodge and Jeep
- (4) Includes Acura, Hummer, Infiniti, Jaguar, Land Rover, Maybach, Morgan, Porsche and Saab
- (5) Includes Isuzu, KIA, Lincoln, Mercury, Mini, Mitsubishi, Scion and Subaru

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We have accounted for all of our dealership acquisitions using the purchase method of accounting and, as a result, we do not include in our consolidated financial statements the results of operations of these dealerships prior to the date they were acquired. Our unaudited condensed consolidated financial statements discussed below reflect the results of operations, financial position and cash flows of each of our dealerships acquired prior to March 31, 2005. As a result of the effects of our acquisitions and other potential factors in the future, the historical consolidated financial information described in "Management's Discussion and Analysis of Financial Condition and Results of Operations" is not necessarily indicative of the results of operations, financial position and cash flows that would have resulted had such acquisitions occurred at the beginning of the periods presented, nor is it indicative of future results of operations, financial position and cash flows.

Results of Operations

Except where otherwise noted, the following discussions are on a same store basis.

Revenues

New Vehicles:

	For the Three Months Ended		Units or \$ Change	% Change
	3/31/2004	3/31/2005		
New Vehicle Units				
Same Store	33,956	34,471	515	1.5%
Acquisitions	240	1,659	1,419	591.3%
Total as Reported	34,196	36,130	1,934	5.7%
New Vehicle Revenue (in thousands)				
Same Store	\$ 985,314	\$ 1,006,674	\$21,360	2.2%
Acquisitions	9,809	72,709	62,900	641.2%
Total as Reported	\$ 995,123	\$ 1,079,383	\$84,260	8.5%
New Vehicle Unit Price				
Same Store	\$ 29,017	\$ 29,204	\$ 187	0.6%

New unit sales at our domestic dealerships decreased by 424 units, or 3.2%, for the quarter ended March 31, 2005 compared to the same period last year, while our import new unit sales increased 939 units, or 4.5%. Industry-wide domestic new unit sales were down 2.7% for the quarter ended March 31, 2005. Import sales in the industry increased 2.8% for the quarter ended March 31, 2005. We expect the retail environment for new vehicles to remain challenging for the remainder of 2005.

Our domestic stores' unit volume benefited from strong fleet sales in the first quarter of 2005, which increased 549 units, or 19.0%. Excluding fleet units, all of our domestic brands experienced lower new retail unit sales volumes. Our Cadillac and Ford stores had the largest decreases in retail units of our domestic brands, decreasing by 394 units, or 14.9%, and 351 units, or 12.2%, respectively. Our Cadillac and Ford retail sales have been negatively impacted by the highly competitive truck and SUV market and unfavorable economic conditions in the Michigan region (due primarily to manufacturer uncertainties) where we have a high concentration of Cadillac stores.

All three of our high volume import brands, Honda, Toyota and BMW, experienced unit sales increases at our stores. Specific increases at our stores include: Honda increased 294 units, or 4.7%; Toyota increased 328 units, or 6.3%; and BMW increased 236 units, or 8.9%. Our import brand stores which experienced volume decreases were VW (down 133 units, or 16.1%), Lexus (down 23 units, or 1.9%) and Nissan (down 31 units, or 3.2%).

Our top performing regions for the quarter ended March 31, 2005 were North Los Angeles (up 284 units, or 14.4%), Oklahoma (up 334 units, or 22.6%) and the South Bay of San Francisco (up 222 units, or 8.8%). Heavy concentrations of import and luxury brand dealerships in North Los Angeles contributed to the increase in that region. The increase in the Oklahoma region can be attributed to improved management and a stabilization of our sales teams. New facilities and improved economic conditions contributed to the increase in the South Bay region. Our Michigan, South Los Angeles and San Diego regions showed the largest declines for the quarter ended March 31, 2005 (down 268 units, or 26.0%, 143 units, or 11.8%, and 81 units, or 7.1%, respectively). Our Michigan, South Los Angeles and San Diego regions are underperforming primarily due to the poor performance of domestic brands in these markets.

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Our domestic dealerships had an average unit price decrease of 2.2% for the quarter ended March 31, 2005. Our GM and Ford stores had unit price decreases of 2.1% and 0.9%, respectively. These price decreases can be attributed to an overly competitive market due to an oversupply of these brands. Our Cadillac stores had an average price per unit increase of \$592 or 1.3%, which was attributed to price increases of two models in particular. Import dealerships had an average price per unit increase of 2.6%. Our Honda, BMW and Lexus dealerships experienced increases in new unit sales price for the quarter ended March 31, 2005 as compared to the same period last year (increased 6.4%, 3.1% and 2.6%, respectively). The price increases were primarily due to the change in sales mix for the quarter compared to the same quarter in 2004. Specifically, Honda had a greater percentage of sales coming from trucks and vans.

Used Vehicles:

	For the Three Months Ended		Units or \$ Change	% Change
	3/31/2004	3/31/2005		
Used Vehicle Units				
Same Store	16,950	16,477	(473)	(2.8)%
Acquisitions	86	857	771	896.5%
Total as Reported	17,036	17,334	298	1.7%
Used Vehicle Revenue (in thousands)				
Same Store	\$ 283,349	\$ 281,921	\$ (1,428)	(0.5)%
Acquisitions	2,308	23,939	21,631	937.2%
Total as Reported	\$ 285,657	\$ 305,860	\$20,203	7.1%
Used Vehicle Unit Price				
Same Store	\$ 16,717	\$ 17,110	\$ 393	2.4%

Used vehicle unit sales decreased primarily due to activity at our domestic stores which were down 582 units, or 7.3%, for the quarter ended March 31, 2005. Our Oklahoma region experienced a significant increase in both units (up 215 units, or 17.9%) and revenues (up \$3.8 million, or 25.0%) despite a large concentration of domestic brands due to improved management and a stabilization of our sales teams. We expect the retail environment for used vehicles to remain challenging to the extent new vehicle incentives remain high. The increase in the average price per unit of 2.4% was attributable to an increase in certified pre-owned ("CPO") sales as a percentage of total used vehicle sales. CPO sales as a percentage of total used vehicle sales increased from 43.9% in the first quarter of 2004 to 47.1% in the first quarter of 2005.

Wholesale Vehicles:

	For the Three Months Ended		Units or \$ Change	% Change
	3/31/2004	3/31/2005		
Wholesale Vehicle Units				
Same Store	13,350	13,022	(328)	(2.5)%
Acquisitions	567	1,242	675	119.0%
Total as Reported	13,917	14,264	347	2.5%
Wholesale Vehicle Revenue (in thousands)				
Same Store	\$ 103,752	\$ 108,440	\$ 4,688	4.5%
Acquisitions	7,344	17,842	10,498	142.9%
Total as Reported	\$ 111,096	\$ 126,282	\$15,186	13.7%
Wholesale Unit Price				
Same Store	\$ 7,772	\$ 8,327	\$ 555	7.1%

Higher revenues realized in the first quarter of 2005 were driven by higher unit sales prices. Favorable wholesale pricing increases followed the increases experienced in used retail sales and were consistent with the industry.

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Parts, Service and Collision Repair ("Fixed Operations"):

	For the Three Months Ended		\$ Change	% Change
	3/31/2004	3/31/2005		
Fixed Operations Revenue (in thousands)				
Same Store	\$ 241,373	\$ 243,555	\$ 2,182	0.9%
Acquisitions	1,522	23,860	22,338	1467.7%
Total as Reported	\$ 242,895	\$ 267,415	\$24,520	10.1%

For the quarter ended March 31, 2005, both parts and service revenue increased over the same period last year and collision repair revenues decreased. A large decrease in wholesale parts revenue was offset by increases in warranty parts and service revenues for the three month period ended March 31, 2005. The wholesale parts decrease (\$1.6 million) was mainly the result of our Ford dealerships decline of \$1.1 million. Our Ford wholesale parts revenues have continued to decrease during 2005 due primarily to the decision to exit the wholesale parts business in Houston. We expect our wholesale parts revenues will continue to decrease in the future. The overall warranty increase was attributable to our BMW dealerships.

Finance, Insurance and Other:

	For the Three Months Ended		\$ Change	% Change
	3/31/2004	3/31/2005		
Finance, Insurance and Other Revenue (in thousands)				
Same Store	\$ 42,225	\$ 43,367	\$1,142	2.7%
Acquisitions	1,105	3,169	2,064	186.8%
Total as Reported	\$ 43,330	\$ 46,536	\$3,206	7.4%
Total F&I per Unit				
Same Store, Excluding				
Fleet Units	\$ 883	\$ 917	\$ 34	3.9%

An overall sales volume increase in new vehicles was responsible for a majority of the increase in finance and insurance revenues for the quarter ended March 31, 2005 as compared to the same period last year. Also contributing to the overall increase was an increase in the sale of other aftermarket products as a result of a more managed approach with an emphasis on the balanced sale of a broader offering of these products.

Gross Profit and Gross Margins

Overall same store gross profit as a percentage of revenues ("gross margin") decreased from 15.8% to 15.7% for the quarter ended March 31, 2005 compared to the same period last year. For the quarter ended March 31, 2005, the new vehicle gross margin decreased 30 bps, which was offset by increases in the used vehicle gross margin (20 bps) and the Fixed Operations gross margin (10 bps). We expect new vehicle margin pressure to continue to the extent that production outpaces consumer demand. Revenue mix also contributed to the decline in overall gross margin for the quarter ended March 31, 2005. As a percentage of revenues, F&I revenues increased by 10 bps. Increases in new vehicle revenue as a percentage of total revenues (30 bps) were offset by decreases in the higher margin yielding used vehicle and Fixed Operations revenues (40 bps and 10 bps, respectively) for the quarter ended March 31, 2005.

Selling, General and Administrative Expenses ("SG&A")

Of the reported SG&A expense increase of \$21.6 million, acquisitions accounted for \$16.1 million, or 74.3%, of the increase, while same store dealerships contributed \$5.5 million, or 25.7%. Hail damage in two of our southeast markets accounted for \$1.2 million of the same store increase. Same store advertising spending increased \$1.7 million due to a focused strategy to increase advertising expenditures for certain brands in specific markets. Same store rent expense increased \$1.4 million due to variable rate leases and facility improvements over the past year. Other same store expenses increased \$1.5 million, or 40 bps, year over year. Higher service loaner expenses, credit card fees, delivery expense and bad debt expenses all contributed to the other expense increase. As a percentage of reported gross profits, reported SG&A expenses increased 140 bps to 80.8% in the first quarter of 2005. Excluding the \$1.2 million in hail damage, reported SG&A as a percentage of reported gross profit increased 100 bps to 80.4%.

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Depreciation and Amortization

Depreciation and amortization expense increased by \$0.5 million, or 14.3%, for the three month period ended March 31, 2005. This increase was due to acquisitions, the completion of leasehold improvement projects and other general capital expenditures.

Interest Expense, Floor Plan

The weighted average floor plan interest rate incurred by continuing dealerships was 3.77% for the quarter ended March 31, 2005, compared to 2.58% for the quarter ended March 31, 2004, which increased interest expense by approximately \$2.6 million. The average notes payable-floor plan balance from continuing dealerships increased to \$972.1 million during the first quarter of 2005 from \$914.0 million during the first quarter of 2004, resulting in increased interest expense of approximately \$0.5 million.

Our floor plan interest expenses are substantially offset by amounts received from manufacturers in the form of floor plan assistance. These payments are credited against our cost of sales upon the sale of the vehicle. During the quarter ended March 31, 2005, the amounts we recognized from floor plan interest expense exceeded our floor plan interest assistance by approximately \$0.4 million. In the quarter ended March 31, 2004, floor plan assistance exceeded floor plan interest expense by approximately \$3.1 million.

Interest Expense, Other

Changes in interest expense, other in the first quarter of 2005 compared to the first quarter of 2004 are summarized in the table below:

	For the Three Months Ended March 31, 2005
	Increase/(decrease) (in millions)
Interest rates –	
• Increase in the average interest rate on the Revolving Credit Facility from 3.91% to 5.31%	\$ 0.8
Debt balances –	
• Higher average balance on the Revolving Credit Facility	0.1
• Assumption of Notes Payable to a Finance Company	0.4
Other factors –	
• Decrease in capitalized interest	0.2
• Incremental interest savings related to floating to fixed interest rate swaps	(1.1)
• Incremental interest expense related to fixed to floating interest rate swaps	0.9
• Increase in other expense, net	0.1
	<u>\$ 1.4</u>

Liquidity and Capital Resources

We require cash to finance acquisition and fund debt service and working capital requirements. We rely on cash flows from operations, borrowings under our various credit facilities and offerings of debt and equity securities to meet these requirements.

Because the majority of our consolidated assets are held by our dealership subsidiaries, the majority of our cash flows from operations is generated by these subsidiaries. As a result, our cash flows and ability to service debt depends to a substantial degree on the results of operations of these subsidiaries and their ability to provide us with cash. Uncertainties in the economic environment as well as uncertainties associated with the ultimate resolution of geopolitical conflicts may therefore affect our overall liquidity.

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Floor Plan Facilities

The weighted average interest rate for our floor plan facilities was 3.77% and 2.58% for the three months ended March 31, 2005 and 2004, respectively. In the first quarter of 2005, we received approximately \$9.2 million in manufacturer assistance, which was approximately \$0.6 million less than the amount we paid for floor plan interest. This resulted in an effective borrowing rate under our floor plan facilities of approximately 0.2%. Interest payments under each of our floor plan facilities are due monthly, and we are generally not required to make principal repayments prior to the sale of the vehicles. We were in compliance with all restrictive covenants as of March 31, 2005.

Long-Term Debt and Credit Facilities

The Revolving Credit Facility: At March 31, 2005, our Revolving Credit Facility had a borrowing limit of \$550.0 million, subject to a borrowing base calculated on the basis of our receivables, inventory and equipment and a pledge of certain additional collateral by one of our affiliates (the borrowing base was approximately \$587.7 million at March 31, 2005). The amount available to be borrowed under the Revolving Credit Facility is reduced on a dollar-for-dollar basis by the cumulative face amount of outstanding letters of credit. At March 31, 2005, we had \$55.5 million in letters of credit outstanding and \$213.9 million of borrowing availability.

Notes Payable to a Finance Company: Three notes payable totaling \$26.6 million in aggregate principal were assumed with the purchase of franchises during 2004 (the "Assumed Notes"). The Assumed Notes bear interest rates from 10.52% to 9.52% (with a weighted average of 10.19%), have a combined monthly principal and interest payment of \$0.3 million and are collateralized by letters of credit with a commercial bank. We recorded the Assumed Notes at fair value using an interest rate of 5.35%. The interest rate used to calculate the fair value was based on a quoted market price for notes with similar terms as of the date of assumption.

At March 31, 2005, the outstanding balance and availability on our long-term debt and credit facilities were as follows (in thousands):

	Interest Rate (1)	Outstanding Balance	Additional Borrowing Availability
Revolving Credit Facility (matures October 2006)	LIBOR + 2.55%	\$ 280,657	\$ 213,870
Senior Subordinated Notes (mature August 2013)	8.625%	\$ 271,996	\$ —
Convertible Senior Subordinated Notes (mature May 2009) (2)	5.25%	\$ 127,627	\$ —
Mortgage Facility:			
Construction Loan (matures December 2007)	LIBOR + 2.25%	\$ —	\$ 50,000(3)
Permanent Loan (matures December 2012)	LIBOR + 2.00%	\$ —	\$ 100,000(3)
Notes Payable to a Finance Company (mature November 2015 through September 2016)	10.19%(4)	\$ 31,726	\$ —

(1) Six-month LIBOR was 3.4% at March 31, 2005.

(2) Notes were not convertible at any time during the three months ended March 31, 2005.

(3) Total combined borrowings under the Construction and Permanent Loans are limited to \$100,000. We do not currently intend to borrow on the Construction and Permanent Loans in the future.

(4) Weighted average rate.

We were in compliance with all of the restrictive and financial covenants under all our long-term debt and credit facilities as of March 31, 2005.

Dealership Acquisitions and Dispositions

In the first three months of 2005, we acquired franchises for an aggregate purchase price of \$11.8 million in cash, net of cash acquired, using cash from operations and borrowings under the Revolving Credit Facility. During the first three months of 2005, we completed two franchise dispositions. These disposals generated cash of \$1.7 million.

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Sale-Leaseback Transactions

In an effort to generate additional cash flow, we typically seek to structure our operations to minimize the ownership of real property. As a result, dealership facilities either constructed by us or obtained in acquisitions are typically sold to third parties in sale-leaseback transactions. The resulting operating leases generally have initial terms of 10-15 years and include a series of five-year renewal options. We have no continuing obligations under these arrangements other than lease payments. During the first three months of 2005, we sold \$1.9 million in dealership facilities in sale-leaseback transactions.

Capital Expenditures

Our capital expenditures include the construction of new dealerships and collision repair centers, building improvements and equipment purchased for use in our dealerships. Capital expenditures in the first three months of 2005 were approximately \$21.7 million, of which approximately \$12.7 million related to the construction of new dealerships and collision repair centers. Once completed, these new dealership facilities and collision repair centers are generally sold in sale-leaseback transactions. Capital expenditures incurred during the first three months of 2005 expected to be sold within a year in sale-leaseback transactions or sold in 2005 were \$15.7 million. We do not expect any significant gains or losses from these sales. As of March 31, 2005, commitments for facilities construction projects totaled approximately \$17.1 million. We expect \$14.4 million of this amount to be financed through future sale-leaseback transactions.

Stock Repurchase Program

As of March 31, 2005, our Board of Directors authorized us to expend up to \$185.0 million to repurchase shares of our Class A common stock or redeem securities convertible into Class A common stock. In the first three months of 2005, we repurchased 67,500 shares for approximately \$1.5 million, which was offset by proceeds received from the exercise of stock options under stock compensation plans of \$2.3 million. As of April 29, 2005, we had \$29.9 million remaining to repurchase shares under our Board authorization.

Dividends

Our Board of Directors approved a quarterly cash dividend of \$0.12 per share for shareholders of record on March 15, 2005, which was paid on April 15, 2005. Our Board of Directors has also approved a quarterly cash dividend of \$0.12 per share for stockholders of record on June 15, 2005, which will be paid on July 15, 2005.

Cash Flows

For the three months ended March 31, 2005, net cash used in operating activities was approximately \$15.5 million which was driven primarily by net income adjusted primarily for non-cash items such as depreciation, and changes in working capital accounts (primarily due to an increase in used vehicle inventories which are not financed under notes payable – floor plan), and, to a lesser extent, amortization and losses on disposals of assets. Cash used in investing activities for the first quarter of 2005 was \$25.8 million, which consisted mostly of capital expenditures on property and equipment and dealership acquisitions, offset somewhat by proceeds received from dealership dispositions and sale-leaseback transactions. Net cash provided by financing activities was \$37.3 million, made up mostly of borrowings under the Revolving Credit Facility of \$42.0 million and issuances of stock under our stock compensation plans of \$2.3 million, which was offset by the payment of dividends of \$5.0 million, purchases of treasury stock of \$1.5 million and the payment of long-term debt of \$0.6 million.

Guarantees

In accordance with the terms of our operating lease agreements, our dealership subsidiaries, acting as lessees, generally agree to indemnify the lessor from certain exposure arising as a result of the use of the leased premises, including environmental exposure and repairs to leased property upon termination of the lease. In addition, we have generally agreed to indemnify the lessor in the event of a breach of the lease by the lessee.

In connection with franchise dispositions, certain of our dealership subsidiaries have assigned or sublet to the buyer their interests in real property leases associated with such dealerships. In general, the subsidiaries retain responsibility for the performance of certain obligations under such leases, including rent payments and repairs to leased property upon termination of the lease, to the extent that the assignee or sublessee does not perform. The total estimated rent payments remaining under such leases as of March 31, 2005 was approximately \$54.9 million. However, in accordance with the terms of the assignment and sublease agreements, the assignees and

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sublessees have generally agreed to indemnify Sonic and its subsidiaries in the event of non-performance. Additionally, in connection with certain dispositions, we have obtained indemnifications from the parent company or owners of these assignees and sublessees in the event of non-performance.

In accordance with the terms of agreements entered into for the sale of our franchises, we generally agree to indemnify the buyer from certain exposure and costs arising subsequent to the date of sale, including environmental exposure and exposure resulting from the breach of representations or warranties made in accordance with the agreement. While our exposure with respect to environmental remediation and repairs is difficult to quantify, we estimate our maximum exposure associated with these general indemnifications was approximately \$21.4 million at March 31, 2005. These indemnifications generally expire within a period of one to three years following the date of sale. The estimated fair value of these indemnifications was not material.

We expect the maximum exposure of these various guarantees to continue to fluctuate as indemnification periods lapse and we dispose of additional franchises.

Future Liquidity Outlook

We believe our best source of liquidity for future growth remains cash flows generated from operations combined with the availability of borrowings under our floor plan financing (or any replacements thereof) and the Revolving Credit Facility. Though uncertainties in the economic environment as well as uncertainties associated with geopolitical conflicts may affect our ability to generate cash from operations, we expect to generate more than sufficient cash flow to fund our debt service, quarterly cash dividends and working capital requirements and any seasonal operating requirements, including our currently anticipated internal growth for our existing businesses, for the foreseeable future. Once these needs are met, we may use remaining cash flow to support our acquisition strategy or repurchase shares of our Class A common stock or publicly-traded debt securities, based on market conditions.

Seasonality

Our operations are subject to seasonal variations. The first and fourth quarters generally contribute less revenue, operating profits and cash flows than the second and third quarters. Weather conditions, the timing of manufacturer incentive programs and model changeovers cause seasonality in new vehicle demand. Parts and service demand remains more stable throughout the year.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

Item 3: Quantitative and Qualitative Disclosures About Market Risk.

Interest Rate Risk

Our variable rate notes payable—floor plan, Revolving Credit Facility borrowings and other variable rate notes expose us to risks caused by fluctuations in the underlying interest rates. The total outstanding balance of such instruments was approximately \$1.4 billion at March 31, 2005. A change of 100 basis points in the underlying interest rate would have caused a change in interest expense of approximately \$3.1 million in the first three months of 2005. Of the total change in interest expense, approximately \$2.1 million in the first three months of 2005 would have resulted from notes payable—floor plan.

Our exposure to notes payable—floor plan is mitigated by floor plan assistance payments received from manufacturers that are generally based on rates similar to those incurred under our floor plan financing arrangements. These payments are capitalized as inventory and charged against cost of sales when the associated inventory is sold. During the three months ended March 31, 2005, the amounts we paid for floor plan interest for both our continuing and discontinued operations exceeded manufacturer floor plan assistance received by approximately \$0.6 million. The effective rate incurred was 0.2%. During the three month period ended March 31, 2004, amounts we received from manufacturer floor plan assistance exceeded our floor plan expense by approximately \$3.2 million. As a result, the effective rate incurred under our floor plan financing arrangements was reduced to 0% after considering these incentives. A change of 100 basis points in the underlying interest rate would have caused estimated changes in floor plan assistance of approximately \$1.8 million in the first three months of 2005.

In addition to our variable rate debt, approximately one-half of our dealership facility lease agreements' monthly lease payments fluctuate based on LIBOR interest rates. Many of our lease agreements have interest rate floors whereby our lease expense would not fluctuate significantly in periods when LIBOR is relatively low. A one percent change in LIBOR would change our annual rent expense by approximately \$1.4 million.

In order to reduce our exposure to market risks from fluctuations in interest rates, we have one interest rate swap agreement (the "Fixed Swap") to effectively convert a portion of our LIBOR-based variable rate debt to a fixed rate. The Fixed Swap agreement will mature June 6, 2006 and has a notional principal of \$100.0 million. Under the terms of the Fixed Swap, we receive interest payments on the notional amount at a rate equal to the one month LIBOR rate, adjusted monthly, and make interest payments at a fixed rate of 4.50%.

We also have five separate interest rate swaps with a total notional amount of \$150.0 million (collectively, the "Variable Swaps") to effectively convert a portion of our fixed rate debt to a LIBOR-based variable rate debt. Under the Variable Swaps' agreements, we receive 8.625% on the respective notional amounts and pay interest payments on the respective notional amounts at a rate equal to the six month LIBOR (in arrears) plus a spread ranging from 3.50% to 3.84% with a weighted average spread of 3.64%. The Variable Swaps expire on August 15, 2013.

Foreign Currency Risk

Similar to other automotive retailers, we purchase certain of our new vehicle and parts inventories from foreign manufacturers. Although we purchase our inventories in U.S. Dollars, our business is subject to foreign exchange rate risk, which may influence automobile manufacturers' ability to provide their products at competitive prices in the United States. To the extent this volatility negatively impacts consumer demand through higher retail prices for our products, this volatility could adversely affect our future operating results.

Item 4: Controls and Procedures.

Our management, under the supervision and with the participation of our principal executive officer and principal financial officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q. There were no changes in our internal control over financial reporting during the past fiscal quarter that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

PART II – OTHER INFORMATION

Item 1: Legal Proceedings.

We are involved, and expect to continue to be involved, in numerous legal proceedings arising in the ordinary course of our business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities.

Several of our Texas dealership subsidiaries have been named in three class action lawsuits against the Texas Automobile Dealers Association (“TADA”) and new vehicle dealerships in Texas that are members of the TADA. Approximately 630 Texas dealerships are named as defendants in two of the actions, and approximately 700 dealerships are named as defendants in the other action. The three actions allege that since 1994, Texas automobile dealerships have deceived customers with respect to a vehicle inventory tax and violated federal antitrust and other laws. In April 2002, in two actions, the Texas state court certified two classes of consumers on whose behalf the actions would proceed. The Texas Court of Appeals has affirmed the trial court’s order of class certification in the state actions, and the Texas Supreme Court issued an order for the second time in September 2004 stating that it would not hear the merits of the defendant’s appeal on class certification. The federal trial court conditionally certified a class of consumers in the federal antitrust case, but on appeal by the defendant dealerships, the U.S. Court of Appeals for the Fifth Circuit reversed the certification of the plaintiff class in October 2004 and remanded the case back to the federal trial court for further proceedings not inconsistent with the Fifth Circuit’s ruling. The plaintiffs may appeal this ruling by the Fifth Circuit.

If the TADA matters are not settled, Sonic and its dealership subsidiaries intend to vigorously defend themselves and assert available defenses. In addition, Sonic may have rights of indemnification with respect to certain aspects of the TADA matters. However, an adverse resolution of the TADA matters may result in the payment of significant costs and damages, which could have a material adverse effect on Sonic’s future results of operations and cash flows.

In addition to the TADA matters described above, we are also involved in numerous other legal proceedings arising out of the conduct of our business. We do not believe that the ultimate resolution of these legal proceedings will have a material adverse effect on our business, financial condition, results of operations, cash flows or prospects. However, the results of these legal proceedings cannot be predicted with certainty, and an unfavorable resolution of one or more of these legal proceedings could have a material adverse effect on our business, financial condition, results of operations, cash flows and prospects.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

Item 2: Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities

The following table sets forth information about the shares of Class A Common Stock we repurchased during the fiscal quarter ended March 31, 2005.

	<u>Total Number of Shares Purchased (1)</u>	<u>Average Price Paid per Share</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)</u>	<u>Approximate Dollar Value of Shares That May Yet Be Purchased Under the Plans or Programs</u>
		(Amounts in Thousands, Except Per Share Amounts)		
January 2005	—	\$ —	—	\$ 32,838
February 2005	—	—	—	32,838
March 2005	68	22.29	68	31,334
Total	68	\$ 22.29	68	\$ 31,334

- (1) All shares repurchased were part of publicly announced share repurchase programs
(2) Our publicly announced Class A Common Stock repurchase authorizations occurred as follows:

	(Amounts in Thousands)
November 1999	\$ 25,000
February 2000	25,000
December 2000	25,000
May 2001	25,000
August 2002	25,000
February 2003	20,000
December 2003	20,000
July 2004	20,000
Total	\$ 185,000

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

Item 6: Exhibits.

(a) Exhibits:

<u>Exhibit No.</u>	<u>Description</u>
31.1	Certification of Mr. E. Lee Wyatt, Jr. pursuant to Rule 13a – 14 (a).
31.2	Certification of Mr. O. Bruton Smith pursuant to Rule 13a – 14 (a).
32.1	Certification of Mr. E. Lee Wyatt, Jr. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Mr. O. Bruton Smith pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.1	Risk Factors.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

Forward Looking Statements

This Quarterly Report on Form 10-Q contains numerous “forward-looking statements” within the meaning of the Private Litigation Securities Reform Act of 1995. These forward looking statements address our future objectives, plans and goals, as well as our intent, beliefs and current expectations regarding future operating performance, and can generally be identified by words such as “may,” “will,” “should,” “believe,” “expect,” “anticipate,” “intend,” “plan,” “foresee,” and other similar words or phrases. Specific events addressed by these forward-looking statements include, but are not limited to:

- future acquisitions;
- industry trends;
- general economic trends, including employment rates and consumer confidence levels;
- vehicle sales rates and same store sales growth;
- our financing plans; and
- our business and growth strategies.

These forward-looking statements are based on our current estimates and assumptions and involve various risks and uncertainties. As a result, you are cautioned that these forward looking statements are not guarantees of future performance, and that actual results could differ materially from those projected in these forward looking statements. Factors which may cause actual results to differ materially from our projections include those risks described in Exhibit 99.1 of this Form 10-Q and elsewhere in this report, as well as:

- our ability to generate sufficient cash flows or obtain additional financing to support acquisitions, capital expenditures, our share repurchase program, and general operating activities;
- the reputation and financial condition of vehicle manufacturers whose brands we represent, and their ability to design, manufacture, deliver and market their vehicles successfully;
- our relationships with manufacturers which may affect our ability to complete additional acquisitions;
- changes in laws and regulations governing the operation of automobile franchises, accounting standards, taxation requirements, and environmental laws;
- general economic conditions in the markets in which we operate, including fluctuations in interest rates, employment levels, the level of consumer spending and consumer credit availability;
- high competition in the automotive retailing industry which not only creates pricing pressures on the products and services we offer, but on businesses we seek to acquire; and
- our ability to successfully integrate recent and potential future acquisitions.

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

EXHIBIT INDEX

<u>Exhibit No.</u>	<u>Description</u>
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32.2	Certification of Mr. O. Bruton Smith pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
99.1	Risk Factors.

CERTIFICATION

I, E. Lee Wyatt, Jr., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sonic Automotive, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2005

By: /s/ E. Lee Wyatt, Jr.

E. Lee Wyatt, Jr.
Executive Vice President, Chief Financial Officer and Treasurer

CERTIFICATION

I, O. Bruton Smith, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Sonic Automotive, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 6, 2005

By: /s/ O. Bruton Smith

O. Bruton Smith,
Chairman and Chief Executive Officer

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Sonic Automotive, Inc. (the "Company") on Form 10-Q for the period ending March 31, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, E. Lee Wyatt, Jr., Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ E. Lee Wyatt, Jr.

E. Lee Wyatt, Jr.
Executive Vice President, Chief
Financial Officer and Treasurer

May 6, 2005

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Sonic Automotive, Inc. (the "Company") on Form 10-Q for the period ending March 31, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, O. Bruton Smith, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ O. Bruton Smith

O. Bruton Smith
Chairman and Chief Executive Officer

May 6, 2005

SONIC AUTOMOTIVE, INC. AND SUBSIDIARIES

RISK FACTORS

Risks Related to Our Indebtedness

Our significant indebtedness could materially adversely affect our financial health, limit our ability to finance future acquisitions and capital expenditures and prevent us from fulfilling our financial obligations.

As of March 31, 2005, our total outstanding indebtedness was approximately \$1,761.5 million, including the following:

- \$280.7 million under a revolving credit facility;
- \$1,050.9 million under standardized secured inventory floor plan facilities;
- \$127.6 million in 5 1/4% convertible senior subordinated notes due 2009 representing \$130.1 million in aggregate principal amount outstanding less unamortized discount of approximately \$2.5 million;
- \$272.0 million in 8 5/8% senior subordinated notes due 2013 representing \$275.0 million in aggregate principal amount outstanding less unamortized net discount of approximately \$3.0 million; and
- \$30.3 million of other secured debt, representing \$23.9 million in aggregate principal amount plus unamortized premium of approximately \$6.4 million.

As of March 31, 2005, we had approximately \$213.9 million available for additional borrowings under a revolving credit facility. We also had approximately \$100.0 million available under a construction/mortgage credit facility for real estate acquisitions and new dealership construction. We also have significant additional capacity under the floor plan facilities. In addition, the indentures relating to our senior subordinated notes, convertible senior subordinated notes and other debt instruments allow us to incur additional indebtedness, including secured indebtedness.

The degree to which we are leveraged could have important consequences to the holders of our securities, including the following:

- our ability to obtain additional financing for acquisitions, capital expenditures, working capital or general corporate purposes may be impaired in the future;
- a substantial portion of our current cash flow from operations must be dedicated to the payment of principal and interest on our indebtedness, thereby reducing the funds available to us for our operations and other purposes;
- some of our borrowings are and will continue to be at variable rates of interest, which exposes us to the risk of increasing interest rates;
- the indebtedness outstanding under our revolving credit facility and floor plan facilities are secured by a pledge of substantially all the assets of our dealerships; and
- we may be substantially more leveraged than some of our competitors, which may place us at a relative competitive disadvantage and make us more vulnerable to changing market conditions and regulations.

In addition, our debt agreements contain numerous covenants that limit our discretion with respect to business matters, including mergers or acquisitions, paying dividends, incurring additional debt, making capital expenditures or disposing of assets.

An acceleration of our obligation to repay all or a substantial portion of our outstanding indebtedness would have a material adverse effect on our business, financial condition or results of operations.

Our revolving credit facility, floor plan facilities and the indenture governing our senior subordinated notes contain numerous financial and operating covenants. A breach of any of these covenants could result in a default under the applicable agreement or indenture. If a default were to occur, we may be unable to adequately finance our operations and the value of our common stock would be materially adversely affected. In addition, a default under one agreement or indenture could result in a default and acceleration of our repayment obligations under the other agreements or indentures, including the indentures governing our outstanding convertible senior subordinated notes and our 8 5/8% senior subordinated notes, under the cross default provisions in those agreements or indentures. If a cross default were to occur, we may not be able to pay our debts or borrow sufficient funds to refinance them. Even if new financing were available, it may not be on terms acceptable to us. As a result of this risk, we could be forced to take actions that we otherwise would not take, or not take actions that we otherwise might take, in order to comply with the covenants in these agreements and indentures.

Our ability to make interest and principal payments when due to holders of our debt securities depends upon the receipt of sufficient funds from our subsidiaries.

Substantially all of our consolidated assets are held by our subsidiaries and substantially all of our consolidated cash flow and net income are generated by our subsidiaries. Accordingly, our cash flow and ability to service debt depends to a substantial degree on the results of operations of subsidiaries and upon the ability of our subsidiaries to provide us with cash. We may receive cash from our subsidiaries in the form of dividends, loans or otherwise. We may use this cash to service our debt obligations or for working capital. Our subsidiaries are separate and distinct legal entities and have no obligation, contingent or otherwise, to distribute cash to us or to make funds available to service debt. In addition, the ability of our subsidiaries to pay dividends or make loans to us are subject to contractual limitations under the floor plan facilities, minimum net capital requirements under manufacturer franchise agreements and laws of the state in which a subsidiary is organized and depend to a significant degree on the results of operations of our subsidiaries and other business considerations.

Risks Related to Our Relationships with Vehicle Manufacturers

Our operations may be adversely affected if one or more of our manufacturer franchise agreements is terminated or not renewed.

Each of our dealerships operates under a franchise agreement with the applicable automobile manufacturer or distributor. Without a franchise agreement, we cannot obtain new vehicles from a manufacturer. As a result, we are significantly dependent on our relationships with these manufacturers.

Manufacturers exercise a great degree of control over the operations of our dealerships through the franchise agreements. The franchise agreements govern, among other things, our ability to purchase vehicles from the manufacturer and to sell vehicles to customers. Each of our franchise agreements provides for termination or non-renewal for a variety of causes, including any unapproved change of ownership or management. Manufacturers may also have a right of first refusal if we seek to sell dealerships.

Actions taken by manufacturers to exploit their superior bargaining position in negotiating the terms of franchise agreements or renewals of these agreements or otherwise could also have a material adverse effect on our results of operations. We cannot assure you that any of our existing franchise agreements will be renewed or that the terms and conditions of such renewals will be favorable to us.

Our sales volume and profit margin on each sale may be materially adversely affected if manufacturers discontinue or change their incentive programs.

Our dealerships depend on the manufacturers for certain sales incentives, warranties and other programs that are intended to promote and support dealership new vehicle sales. Manufacturers routinely modify their incentive programs in response to changing market conditions. Some of the key incentive programs include:

- customer rebates or below market financing on new vehicles;
- dealer incentives on new vehicles;
- warranties on new and used vehicles; and
- sponsorship of used vehicle sales by authorized new vehicle dealers.

Manufacturers are currently offering very favorable incentives to potential customers. A reduction or discontinuation of a manufacturer's incentive programs may materially adversely affect our profitability.

We depend on manufacturers to supply us with sufficient numbers of popular and profitable new models.

Manufacturers typically allocate their vehicles among dealerships based on the sales history of each dealership. Supplies of popular new vehicles may be limited by the applicable manufacturer's production capabilities. Popular new vehicles that are in limited supply typically produce the highest profit margins. We depend on manufacturers to provide us with a desirable mix of popular new vehicles. Our operating results may be materially adversely affected if we do not obtain a sufficient supply of these vehicles.

Adverse conditions affecting one or more key manufacturers may negatively impact our profitability.

During the first quarter of 2005, approximately 68.9% of our new vehicle revenue was derived from the sale of new vehicles manufactured by Ford, Honda, General Motors (including Cadillac), BMW and Toyota. Our success depends to a great extent on these manufacturers’:

- financial condition;
- marketing;
- vehicle design;
- publicity concerning a particular manufacturer or vehicle model;
- production capabilities;
- management;
- reputation; and
- labor relations.

Events such as labor strikes that may adversely affect a manufacturer may also adversely affect us. In particular, labor strikes at a manufacturer that continue for a substantial period of time could have a material adverse effect on our business. Similarly, the delivery of vehicles from manufacturers at a time later than scheduled, which may occur particularly during periods of new product introductions, could limit sales of those vehicles during those periods. This has been experienced at some of our dealerships from time to time. Adverse conditions affecting these and other important aspects of manufacturers’ operations and public relations may adversely affect our ability to sell their automobiles and, as a result, significantly and detrimentally affect our profitability.

Manufacturer stock ownership restrictions may impair our ability to maintain or renew franchise agreements or issue additional equity.

Some of our franchise agreements prohibit transfers of any ownership interests of a dealership and, in some cases, its parent, without prior approval of the applicable manufacturer. A number of manufacturers impose restrictions on the transferability of our Class A common stock and our ability to maintain franchises if a person acquires a significant percentage of the voting power of our common stock. Our existing franchise agreements could be terminated if a person or entity acquires a substantial ownership interest in us or acquires voting power above certain levels without the applicable manufacturer’s approval. Violations of these levels by an investor are generally outside of our control and may result in the termination or non-renewal of existing franchise agreements or impair our ability to negotiate new franchise agreements for dealerships we acquire. In addition, if we cannot obtain any requisite approvals on a timely basis, we may not be able to issue additional equity or otherwise raise capital on terms acceptable to us. These restrictions may also prevent or deter a prospective acquiror from acquiring control of us. This could adversely affect the market price of our Class A common stock.

The current holders of our Class B common stock maintain voting control over us. However, we are unable to prevent our stockholders from transferring shares of our common stock, including transfers by holders of the Class B common stock. If such transfer results in a change in control, it could result in the termination or non-renewal of one or more of our existing franchise agreements, the triggering of provisions in our agreements with certain manufacturers requiring us to sell our dealerships franchised with such manufacturers and/or a default under our credit arrangements.

Manufacturers’ restrictions on acquisitions could limit our future growth.

We are required to obtain the approval of the applicable manufacturer before we can acquire an additional dealership franchise of that manufacturer. In determining whether to approve an acquisition, manufacturers may consider many factors such as our financial condition and manufacturer-determined consumer satisfaction index, or “CSI” scores. Obtaining manufacturer approval of acquisitions also takes a significant amount of time, typically three to five months. We cannot assure you that manufacturers will approve future acquisitions or do so on a timely basis, which could impair the execution of our acquisition strategy.

Certain manufacturers also limit the number of its dealerships that we may own, our national market share of that manufacturer’s products or the number of dealerships we may own in a particular geographic area. In addition, under an applicable franchise agreement or under state law, a manufacturer may have a right of first refusal to acquire a dealership that we seek to acquire.

A manufacturer may condition approval of an acquisition on the implementation of material changes in our operations or extraordinary corporate transactions, facilities improvements or other capital expenditures. If we are unable or unwilling to comply with these conditions, we may be required to sell the assets of that manufacturer’s dealerships or terminate our franchise agreement.

Our dealers depend upon vehicle sales and, therefore, their success depends in large part upon customer demand for the particular vehicles they carry.

The success of our dealerships depends in large part on the overall success of the vehicle lines they carry. New vehicle sales generate the majority of our total revenue and lead to sales of higher-margin products and services such as finance and insurance products and parts and service operations. Although we have sought to limit our dependence on any one vehicle brand, we have focused our new vehicle sales operations in mid-line import and luxury brands.

Our failure to meet a manufacturer's consumer satisfaction, financial and sales performance requirements may adversely affect our ability to acquire new dealerships and our profitability.

Many manufacturers attempt to measure customers' satisfaction with their sales and warranty service experiences through CSI scores. The components of CSI vary from manufacturer to manufacturer and are modified periodically. Franchise agreements also may impose financial and sales performance standards. Under our agreements with certain manufacturers, a dealership's CSI scores, sales and financial performance may be considered a factor in evaluating applications for additional dealership acquisitions. From time to time, some of our dealerships have had difficulty meeting various manufacturers' CSI requirements or performance standards. We cannot assure you that our dealerships will be able to comply with these requirements in the future. A manufacturer may refuse to consent to an acquisition of one of its franchises if it determines our dealerships do not comply with its CSI requirements or performance standards, which could impair the execution of our acquisition strategy. In addition, we receive incentive payments from the manufacturers based, in part, on CSI scores, which could be materially adversely affected if our CSI scores decline.

If state dealer laws are repealed or weakened, our dealerships will be more susceptible to termination, non-renewal or renegotiation of their franchise agreements.

State dealer laws generally provide that a manufacturer may not terminate or refuse to renew a franchise agreement unless it has first provided the dealer with written notice setting forth good cause and stating the grounds for termination or nonrenewal. Some state dealer laws allow dealers to file protests or petitions or attempt to comply with the manufacturer's criteria within the notice period to avoid the termination or nonrenewal. Though unsuccessful to date, manufacturers' lobbying efforts may lead to the repeal or revision of state dealer laws. If dealer laws are repealed in the states in which we operate, manufacturers may be able to terminate our franchises without providing advance notice, an opportunity to cure or a showing of good cause. Without the protection of state dealer laws, it may also be more difficult for our dealers to renew their franchise agreements upon expiration.

In addition, these laws restrict the ability of automobile manufacturers to directly enter the retail market in the future. If manufacturers obtain the ability to directly retail vehicles and do so in our markets, such competition could have a material adverse effect on us.

Risks Related to Our Acquisition Strategy

Failure to effectively integrate acquired dealerships with our existing operations could adversely affect our future operating results.

Our future operating results depend on our ability to integrate the operations of recently acquired dealerships, as well as dealerships we acquire in the future, with our existing operations. In particular, we need to integrate our management information systems, procedures and organizational structures, which can be difficult. Our growth strategy has focused on the pursuit of strategic acquisitions that either expand or complement our business.

We cannot assure you that we will effectively and profitably integrate the operations of these dealerships without substantial costs, delays or operational or financial problems, due to:

- the difficulties of managing operations located in geographic areas where we have not previously operated;
- the management time and attention required to integrate and manage newly acquired dealerships;
- the difficulties of assimilating and retaining employees; and
- the challenges of keeping customers.

These factors could have a material adverse effect on our financial condition and results of operations.

We may not adequately anticipate all of the demands that growth through acquisitions will impose.

The automobile retailing industry is considered a mature industry in which minimal growth is expected in total unit sales. Accordingly, our ability to generate higher revenue and earnings in future periods depends in large part on our ability to acquire additional dealerships, manage geographic expansion, control costs in our operations and consolidate both past and future dealership acquisitions into our existing operations. In pursuing a strategy of acquiring other dealerships, we face risks commonly encountered with growth through acquisitions. These risks include, but are not limited to:

- incurring significantly higher capital expenditures and operating expenses;

-
- failing to assimilate the operations and personnel of acquired dealerships;
 - entering new markets with which we are unfamiliar;
 - potential undiscovered liabilities and operational difficulties at acquired dealerships;
 - disrupting our ongoing business;
 - diverting our limited management resources;
 - failing to maintain uniform standards, controls and policies;
 - impairing relationships with employees, manufacturers and customers as a result of changes in management;
 - increased expenses for accounting and computer systems, as well as integration difficulties;
 - failure to obtain a manufacturer's consent to the acquisition of one or more of its dealership franchises or renew the franchise agreement on terms acceptable to us; and
 - incorrectly valuing entities to be acquired.

We may not adequately anticipate all of the demands that growth will impose on our systems, procedures and structures.

We may not be able to capitalize on acquisition opportunities because our financial resources available for acquisitions are limited.

We intend to finance our acquisitions with cash generated from operations, through issuances of our stock or debt securities and through borrowings under credit arrangements. We may not be able to obtain additional financing by issuing stock or debt securities due to the market price of our Class A common stock, overall market conditions or the need for manufacturer consent to the issuance of equity securities. Using cash to complete acquisitions could substantially limit our operating or financial flexibility. If we are unable to obtain financing on acceptable terms, we may be required to reduce the scope of our presently anticipated expansion, which could materially adversely affect our overall growth strategy.

In addition, we are dependent to a significant extent on our ability to finance our new vehicle inventory with "floor plan financing." Floor plan financing arrangements allow us to borrow money to buy a particular vehicle from the manufacturer and pay off the loan when we sell that particular vehicle. We must obtain new floor plan financing or obtain consents to assume existing floor plan financing in connection with our acquisition of dealerships.

Substantially all the assets of our dealerships are pledged to secure our floor plan indebtedness and the indebtedness under the revolving credit facility. In addition, substantially all the real property and assets of our subsidiaries that are constructing new dealerships are pledged under our construction/mortgage facility with Toyota Credit. These pledges may impede our ability to borrow from other sources. Moreover, because Toyota Credit is associated with Toyota Motor Sales, U.S.A., Inc., any deterioration of our relationship with one could adversely affect our relationship with the other. The same is true of our relationships with Chrysler, GM and Ford and the floor plan financing divisions of each of these manufacturers.

We may not be able to continue executing our acquisition strategy without the costs of future acquisitions escalating.

We have grown our business primarily through acquisitions. We may not be able to consummate any future acquisitions at acceptable prices and terms or identify suitable candidates. In addition, increased competition for acquisition candidates could result in fewer acquisition opportunities for us and higher acquisition prices. The magnitude, timing, pricing and nature of future acquisitions will depend upon various factors, including:

- the availability of suitable acquisition candidates;
- competition with other dealer groups for suitable acquisitions;
- the negotiation of acceptable terms;

- our financial capabilities;
- our stock price; and
- the availability of skilled employees to manage the acquired companies.

We may not be able to determine the actual financial condition of dealerships we acquire until after we complete the acquisition and take control of the dealerships.

The operating and financial condition of acquired businesses cannot be determined accurately until we assume control. Although we conduct what we believe to be a prudent level of investigation regarding the operating and financial condition of the businesses we purchase, in light of the circumstances of each transaction, an unavoidable level of risk remains regarding the actual operating condition of these businesses. Similarly, many of the dealerships we acquire, including our largest acquisitions, do not have financial statements audited or prepared in accordance with generally accepted accounting principles. We may not have an accurate understanding of the historical financial condition and performance of our acquired entities. Until we actually assume control of business assets and their operations, we may not be able to ascertain the actual value or understand the potential liabilities of the acquired entities and their operations.

Although O. Bruton Smith, our chairman and chief executive officer, has previously assisted us with obtaining acquisition financing, we cannot assure you that he will be willing or able to do so in the future.

Our obligations under the revolving credit facility are secured with a pledge of shares of common stock of Speedway Motorsports, Inc., a publicly traded owner and operator of automobile racing facilities. These shares of Speedway Motorsports common stock are beneficially owned by Sonic Financial Corporation, an entity controlled by Mr. Smith. Presently, the \$550.0 million borrowing limit of the revolving credit facility is subject to a borrowing base calculation that is based, in part, on the value of the Speedway Motorsports shares pledged by Sonic Financial. Consequently, a withdrawal of this pledge by Sonic Financial or a significant decrease in the value of Speedway Motorsports common stock could reduce the amount we can currently borrow under the revolving credit facility.

Mr. Smith has also guaranteed additional indebtedness incurred to complete certain dealership acquisitions. Mr. Smith may not be willing or able to provide similar guarantees or credit support in the future. This could impair our ability to obtain acquisition financing on favorable terms.

Risks Related to the Automotive Retail Industry

Increasing competition among automotive retailers reduces our profit margins on vehicle sales and related businesses. Further, the use of the Internet in the car purchasing process could materially adversely affect us.

Automobile retailing is a highly competitive business. Our competitors include publicly and privately owned dealerships, some of which are larger and have greater financial and marketing resources than we do. Many of our competitors sell the same or similar makes of new and used vehicles that we offer in our markets at competitive prices. We do not have any cost advantage in purchasing new vehicles from manufacturers due to economies of scale or otherwise. In addition, the popularity of short-term vehicle leasing in the past few years also has resulted, as these leases expire, in a large increase in the number of late model used vehicles available in the market, which puts added pressure on new and used vehicle margins. We typically rely on advertising, merchandising, sales expertise, service reputation and dealership location to sell new vehicles. Our revenues and profitability could be materially adversely affected if manufacturers decide to enter the retail market directly.

Our financing and insurance ("F&I") business and other related businesses, which have higher margins than sales of new and used vehicles, are subject to strong competition from various financial institutions and other third parties.

This competition is increasing as these products are now being marketed and sold over the Internet.

The Internet has become a significant part of the sales process in our industry. Customers are using the Internet to compare pricing for cars and related F&I services, which may further reduce margins for new and used cars and profits for related F&I services. If Internet new vehicle sales are allowed to be conducted without the involvement of franchised dealers, our business could be materially adversely affected. In addition, other franchise groups have aligned themselves with Internet car sellers or are investing heavily in the development of their own Internet capabilities, which could materially adversely affect our business.

Our franchise agreements do not grant us the exclusive right to sell a manufacturer's product within a given geographic area. Our revenues or profitability could be materially adversely affected if any of our manufacturers award franchises to others in the same markets where we operate or if existing franchised dealers increase their market share in our markets.

As we seek to acquire dealerships in new markets, we may face increasingly significant competition as we strive to gain market share through acquisitions or otherwise. Our gross margins may decline over time as we expand into markets where we do not have a leading position.

Our business will be harmed if overall consumer demand suffers from a severe or sustained downturn.

Our business is heavily dependent on consumer demand and preferences. Our revenues will be materially and adversely affected if there is a severe or sustained downturn in overall levels of consumer spending. Retail vehicle sales are cyclical and historically have experienced periodic downturns characterized by oversupply and weak demand. These cycles are often dependent on general economic conditions and consumer confidence, as well as the level of discretionary personal income and credit availability. Future recessions may have a material adverse effect on our retail business, particularly sales of new and used automobiles. In addition, severe or sustained increases in gasoline prices may lead to a reduction in automobile purchases or a shift in buying patterns from luxury and sport utility vehicle models (which typically provide high margins to retailers) to smaller, more economical vehicles (which typically have lower margins).

A decline of available financing in the sub-prime lending market has, and may continue to, adversely affect our sales of used vehicles.

A significant portion of vehicle buyers, particularly in the used car market, finance their purchases of automobiles. Sub-prime lenders have historically provided financing for consumers who, for a variety of reasons including poor credit histories and lack of down payment, do not have access to more traditional finance sources. Our recent experience suggests that sub-prime lenders have tightened their credit standards and may continue to apply these higher standards in the future. This has adversely affected our used vehicle sales. If sub-prime lenders continue to apply these higher standards or if there is any further tightening of credit standards used by sub-prime lenders or if there is any additional decline in the overall availability of credit in the sub-prime lending market, the ability of these consumers to purchase vehicles could be limited which could have a material adverse effect on our used car business, revenues and profitability.

Our business may be adversely affected by import product restrictions and foreign trade risks that may impair our ability to sell foreign vehicles profitably.

A significant portion of our new vehicle business involves the sale of vehicles, parts or vehicles composed of parts that are manufactured outside the United States. As a result, our operations are subject to customary risks of importing merchandise, including fluctuations in the relative values of currencies, import duties, exchange controls, trade restrictions, work stoppages and general political and socio-economic conditions in other countries. The United States or the countries from which our products are imported may, from time to time, impose new quotas, duties, tariffs or other restrictions, or adjust presently prevailing quotas, duties or tariffs, which may affect our operations and our ability to purchase imported vehicles and/or parts at reasonable prices.

The seasonality of our business magnifies the importance of second and third quarter operating results.

Our business is subject to seasonal variations in revenues. In our experience, demand for automobiles is generally lower during the first and fourth quarters of each year. We therefore receive a disproportionate amount of revenues generally in the second and third quarters and expect our revenues and operating results to be generally lower in the first and fourth quarters. Consequently, if conditions surface during the second and third quarters that impair vehicle sales, such as higher fuel costs, depressed economic conditions or similar adverse conditions, our revenues for the year could be disproportionately adversely affected.

General Risks Related to Investing in Our Securities

Concentration of voting power and anti-takeover provisions of our charter, Delaware law and our dealer agreements may reduce the likelihood of any potential change of control.

Our common stock is divided into two classes with different voting rights. This dual class stock ownership allows the present holders of the Class B common stock to control us. Holders of Class A common stock have one vote per share on all matters. Holders of Class B common stock have 10 votes per share on all matters, except that they have only one vote per share on any transaction proposed by the Board of Directors or a Class B common stockholder or otherwise benefiting the Class B common stockholders constituting a:

- “going private” transaction;
- disposition of substantially all of our assets;
- transfer resulting in a change in the nature of our business; or
- merger or consolidation in which current holders of common stock would own less than 50% of the common stock following such transaction.

The holders of Class B common stock currently hold less than a majority of our outstanding common stock, but a majority of our voting power. This may prevent or discourage a change of control of us even if the action was favored by holders of Class A common stock.

Our charter and bylaws make it more difficult for our stockholders to take corporate actions at stockholders' meetings. In addition, options under our 1997 Stock Option Plan and 2004 Stock Incentive Plan become immediately exercisable on a change in control. Delaware law also makes it difficult for stockholders who have recently acquired a large interest in a company to consummate a business combination transaction with the company against its directors' wishes. Finally, restrictions imposed by our dealer agreements may impede or prevent any potential takeover bid. Generally, our franchise agreements allow the manufacturers the right to terminate the agreements upon a change of control of our company and impose restrictions upon the transferability of any significant percentage of our stock to any one person or entity who may be unqualified, as defined by the manufacturer, to own one of its dealerships. The inability of a person or entity to qualify with one or more of our manufacturers may prevent or seriously impede a potential takeover bid. In addition, provisions of our lending arrangements create an event of default on a change in control. These agreements, corporate governance documents and laws may have the effect of delaying or preventing a change in control or preventing stockholders from realizing a premium on the sale of their shares if we were acquired.

The outcome of legal and administrative proceedings we are or may become involved in could have an adverse effect on our business, results of operations and profitability.

Several private civil actions filed against Sonic Automotive, Inc. and several of our dealership subsidiaries purport to represent classes of customers as potential plaintiffs, and make allegations that certain products sold in the finance and insurance departments were done so in a deceptive or otherwise illegal manner. A motion for class certification has been filed in one of those private civil actions, although no order certifying a class has been entered in any of the lawsuits. The civil action in which the motion for class certification has been filed purports to represent a class of customers of all of our Florida dealership subsidiaries. We are vigorously opposing this motion for class certification. Another one of these private civil actions has been filed in South Carolina state court against Sonic Automotive, Inc. and 10 of our South Carolina subsidiaries. We have been advised that the plaintiffs' attorneys in this South Carolina private civil action intend to file private civil class actions against Sonic Automotive, Inc. and certain of its subsidiaries in other states. This group of plaintiffs' attorneys has filed another one of these private civil class action lawsuits in state court in North Carolina seeking certification of a multi-state class of plaintiffs. Another one of these private civil actions has been filed in Tennessee state court against Sonic Automotive, Inc. and one of our Tennessee subsidiaries. Another one of these private civil actions has been filed in Florida state court against Sonic Automotive, Inc. and two of our Florida subsidiaries. This lawsuit also names as a defendant the administrator of the settlement agreement reached between two of our Florida subsidiaries, and the Florida Department of Financial Affairs and Attorney General's office. This private civil action alleges, among other things, that the settlement was unfair to the customers who were offered refunds through the settlement with the Florida Department of Financial Services and Attorney General's office.

In September of 2002, the Los Angeles County District Attorney's office served a search warrant on one of our wholly-owned dealership subsidiaries located in Los Angeles County relating to alleged deceptive practices of the dealership's finance and insurance department. Our dealership is cooperating with the District Attorney in its investigation. No charges have been filed and no proceedings have been instituted to date by the District Attorney. A private civil action has also been filed against the dealership stating allegations similar to those underlying the District Attorney's investigation. The plaintiffs in this private civil action purport to represent a class of customers as potential plaintiffs, although no motion for class certification has been filed.

In December 2003, the North Carolina Attorney General's office notified us that it had initiated an inquiry into the sales practices of our North Carolina dealerships following a negative media report on our company. We are cooperating with the North Carolina Attorney General's office in its inquiry. No charges have been filed and no proceedings have been instituted to date by the North Carolina Attorney General's Office.

Because the respective investigations by the Los Angeles County District Attorney's Office and North Carolina Attorney General's Office are continuing and have not resulted in formal charges to date, and because the private civil actions described above are also in the early stages of litigation, we cannot assure you as to the outcomes of these proceedings. We intend to vigorously defend ourselves and assert available defenses with respect to each of the foregoing matters, and do not believe that the ultimate resolution of these matters will have a material adverse affect on our business, results of operations, financial condition, cash flows or prospects.

Furthermore, several of our Texas dealership subsidiaries have been named in three class action lawsuits brought against the Texas Automobile Dealers Association ("TADA") and new vehicle dealerships in Texas that are members of the TADA. Approximately 630 Texas dealerships are named as defendants in two of the actions, and approximately 700 Texas dealerships are named as defendants in the other action. The three actions allege that since January 1994, Texas automobile dealerships have deceived customers with respect to a vehicle inventory tax and violated federal antitrust and other laws. In April 2002, in two actions the Texas state court certified two classes of consumers on whose behalf the actions would proceed. The Texas Court of Appeals has affirmed the trial court's order of class certification in the state actions, and the Texas Supreme Court issued an order for the second

time in September 2004 stating that it would not hear the merits of the defendant's appeal on class certification. The federal trial court conditionally certified a class of consumers in the federal antitrust case, but on appeal by the defendant dealerships, the U.S. Court of Appeals for the Fifth Circuit reversed the certification of the plaintiff class in October 2004 and remanded the case back to the federal trial court for further proceedings not inconsistent with the Fifth Circuit's ruling. The plaintiffs in the federal lawsuit are seeking to have the U.S. Supreme Court hear an appeal of the Fifth Circuit's ruling that reversed the federal trial court's class certification order.

If the TADA matters are not settled, Sonic and its dealership subsidiaries intend to vigorously defend themselves and assert available defenses. In addition, Sonic may have rights of indemnification with respect to certain aspects of the TADA matters. However, an adverse resolution of the TADA matters may result in the payment of significant costs and damages, which could have a material adverse effect on Sonic's future results of operations and cash flows.

Finally, we are involved, and expect to continue to be involved, in numerous other legal proceedings arising out of the conduct of our business, including litigation with customers, employment related lawsuits, contractual disputes, class actions, purported class actions and actions brought by governmental authorities. The results of these matters cannot be predicted with certainty, and an unfavorable resolution of one or more of these matters, including the matters specifically discussed above, could have a material adverse effect on our business, financial condition, results of operations, cash flows and prospects.

Our business may be adversely affected by claims alleging violations of laws and regulations in our advertising, sales and finance and insurance activities.

Our business is highly regulated. In the past several years, private plaintiffs and state attorney generals have increased their scrutiny of advertising, sales, and finance and insurance activities in the sale and leasing of motor vehicles. The conduct of our business is subject to numerous federal, state and local laws and regulations regarding unfair, deceptive and/or fraudulent trade practices (including advertising, marketing, sales, insurance, repair and promotion practices), truth-in-lending, consumer leasing, fair credit practices, equal credit opportunity, privacy, insurance, motor vehicle finance, installment finance, closed-end credit, usury and other installment sales. Claims arising out of actual or alleged violations of law may be asserted against us or any of our dealers by individuals, either individually or through class actions, or by governmental entities in civil or criminal investigations and proceedings. Such actions may expose us to substantial monetary damages and legal defense costs, injunctive relief and criminal and civil fines and penalties, including suspension or revocation of our licenses and franchises to conduct dealership operations.

Our business may be adversely affected by unfavorable conditions in our local markets, even if those conditions are not prominent nationally.

Our performance is subject to local economic, competitive and other conditions prevailing in geographic areas where we operate. For example, our current results of operations depend substantially on general economic conditions and consumer spending habits in the Southeast and in our Northern California and Houston markets. Sales in our Northern California and Houston markets represented approximately 30.5% of our sales for the three months ended March 31, 2005. We may not be able to expand geographically and any geographic expansion may not adequately insulate us from the adverse effects of local or regional economic conditions.

The loss of key personnel and limited management and personnel resources could adversely affect our operations and growth.

Our success depends to a significant degree upon the continued contributions of our management team, particularly our senior management, and service and sales personnel. Additionally, manufacturer franchise agreements may require the prior approval of the applicable manufacturer before any change is made in franchise general managers. We do not have employment agreements with certain members of our senior management team, our dealership managers and other key dealership personnel. Consequently, the loss of the services of one or more of these key employees could have a material adverse effect on our results of operations.

In addition, as we expand we may need to hire additional managers. The market for qualified employees in the industry and in the regions in which we operate, particularly for general managers and sales and service personnel, is highly competitive and may subject us to increased labor costs during periods of low unemployment. The loss of the services of key employees or the inability to attract additional qualified managers could have a material adverse effect on our results of operations. In addition, the lack of qualified management or employees employed by potential acquisition candidates may limit our ability to consummate future acquisitions.

Governmental regulation and environmental regulation compliance costs may adversely affect our profitability.

We are subject to a wide range of federal, state and local laws and regulations, such as local licensing requirements, retail financing and consumer protection laws and regulations, and wage-hour, anti-discrimination and other employment practices laws and regulations. Our facilities and operations are also subject to federal, state and local laws and regulations relating to environmental protection and human health and safety, including those governing wastewater discharges, air emissions, the operation and removal of underground and aboveground storage tanks, the use, storage, treatment, transportation, release, recycling and disposal of solid and hazardous materials and wastes and the cleanup of contaminated property or water. The violation of these laws and regulations can

result in administrative, civil or criminal penalties against us or in a cease and desist order against our operations that are not in compliance. Our future acquisitions may also be subject to regulation, including antitrust reviews. We believe that we comply in all material respects with all laws and regulations applicable to our business, but future regulations may be more stringent and require us to incur significant additional compliance costs.

Our past and present business operations are subject to environmental laws and regulations. We may be required by these laws to pay the full amount of the costs of investigation and/or remediation of contaminated properties, even if we are not at fault for disposal of the materials or if such disposal was legal at the time. Like many of our competitors, we have incurred, and will continue to incur, capital and operating expenditures and other costs in complying with these laws and regulations. In addition, soil and groundwater contamination exists at certain of our properties. We cannot assure you that our other properties have not been or will not become similarly contaminated. In addition, we could become subject to potentially material new or unforeseen environmental costs or liabilities because of our acquisitions.

Potential conflicts of interest between us and our officers or directors could adversely affect our future performance.

O. Bruton Smith serves as the chairman and chief executive officer of Speedway Motorsports. Accordingly, we compete with Speedway Motorsports for the management time of Mr. Smith.

We have in the past and will likely in the future enter into transactions with Mr. Smith, entities controlled by Mr. Smith or our other affiliates. We believe that all of our existing arrangements with affiliates are as favorable to us as if the arrangements were negotiated between unaffiliated parties, although the majority of these transactions have neither been independently verified in that regard nor are likely to be so verified in the future. Potential conflicts of interest could arise in the future between us and our officers or directors in the enforcement, amendment or termination of arrangements existing between them.

An impairment of our goodwill could have a material adverse impact on our earnings.

Pursuant to applicable accounting pronouncements, we test goodwill for impairment annually or more frequently if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. We describe the process for testing goodwill more thoroughly in our Annual Report on Form 10-K under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations—Use of Estimates and Critical Accounting Policies." If we determine that the amount of our goodwill is impaired at any point in time, we will be required to reduce goodwill on our balance sheet. A reduction in the amount of goodwill on our balance sheet will require us to record a non-cash impairment charge against our earnings for the period in which the impairment of goodwill occurred. This would have a material adverse impact on our earnings for that period.

Poor performance in one or more of our geographic divisions could constitute an event or change in circumstances for purposes of determining whether the fair value of our goodwill has been reduced below the carrying amount. We would therefore be required to test our goodwill for impairment. As of March 31, 2005, our balance sheet reflected a carrying amount of approximately \$1,072.0 million in goodwill, which was allocated between four geographic reporting units. If the goodwill in any of our reporting units is impaired, we will record a significant non-cash impairment charge that would likely have a material adverse effect on our earnings for the period in which the impairment of goodwill occurred.